97TH CONGRESS
2d Session

HOUSE OF REPRESENTATIVES

REPORT
No. 97-833

# REDUCTION IN RATE OF CERTAIN TAXES PAID TO VIRGIN ISLANDS

SEPTEMBER 16, 1982.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed.

Mr. ROSTENKOWSKI, from the Committee on Ways and Means, submitted the following

## REPORT

[To accompany H.R. 7093]

The Committee on Ways and Means to whom was referred the bill (H.R. 7093) to amend the Internal Revenue Code of 1954 to reduce the rate of certain taxes paid to the Virgin Islands on Virgin Islands source income, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.

## I. SUMMARY

The Treasury and the Government of the Virgin Islands take the position that present law imposes a 30-percent tax on the non-Virgin Islands recipient of certain Virgin Islands source passive investment income, and that present law also imposes withholding at the source by the V.I. payor of such income. The bill will reduce this tax to 10 percent when the recipient is a U.S. individual or corporation and impose a corresponding withholding obligation on the V.I. payor of such income. The bill will allow the V.I. Government further to reduce this 10-percent rate in its discretion. The bill will not affect payments of V.I. source passive income to non-U.S. persons.

## II. EXPLANATION OF THE BILL

### *Present Law*

#### *Virgin Islands taxation in general*

Under the Revised Organic Act, in the Virgin Islands, the U.S. Internal Revenue Code is generally applied as the local territorial

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tax law, except that tax proceeds are paid into the treasury of the Virgin Islands. This system has been interpreted to require that in applying the Internal Revenue Code in the Virgin Islands, the name "Virgin Islands" is generally substituted, whenever appropriate, for the name "United States" where it appears in the U.S. Code (the so-called "mirror image" system).

Corporate and individual "inhabitants" of the Virgin Islands are taxed on their worldwide income by the Virgin Islands and are exempt from any income tax liability to the Federal Treasury, even on their U.S.-source income. All corporations chartered in the Virgin Islands are considered to be inhabitants of the Virgin Islands. In certain circumstances, a United States corporation may also qualify as an inhabitant of the Virgin Islands.

The U.S. Internal Revenue Code limits the power of the Virgin Islands government to reduce its income tax (sec. 934). The Virgin Islands may not reduce its taxes attributable to income derived from sources within the United States. With respect to non-U.S. source income, the Virgin Islands may not reduce its corporate tax except to U.S. and V.I. corporations that meet a so-called "80–50 test." This test allows the Virgin Islands to reduce taxes only for those U.S. and V.I. corporations that have derived for the past three taxable years (or applicable part thereof) at least 80 percent of their gross income from V.I. sources and at least 50 percent[1] of their gross income from the active conduct of a trade or business within the Virgin Islands. Acting within the constraint of the 80–50 test, the Government of the Virgin Islands has established further criteria for tax reductions, such as a $50,000 minimum investment and certain employment criteria.

***Taxation of passive income in the Virgin Islands***

U.S. law generally imposes a 30-percent tax on the gross amount of dividends, interest, royalties, and other fixed or determinable annual or periodic income (hereinafter sometimes referred to as passive investment income) paid by U.S. persons to non-resident aliens and foreign corporations when that income is not effectively connected with the conduct of a U.S. trade or business by the foreign person. This 30-percent rate is often reduced, or eliminated, by income tax treaties. U.S. law also generally imposes on the payor of such passive investment income a duty to withhold the tax due (secs. 1441 and 1442).

Under the mirror system, the Virgin Islands imposes a similar 30-percent tax on passive investment income paid by V.I. persons to non-V.I. persons, including U.S. persons. The Virgin Islands cannot now forgive this tax, since the tax is upon the recipient and not upon the company operating in the Virgin Islands. A U.S. recipient of passive income from the Virgin Islands may generally take a foreign tax credit for any such tax (subject to limits) against

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[1] Under the Tax Equity and Fiscal Responsibility Act of 1982, Public Law 97-248, the percentage of a corporation's gross income that must be derived from the active conduct of a trade or business in the Virgin Islands is increased from 50 percent to 65 percent. This increase will be phased in over three years. For taxable years beginning after Dec. 31, 1982, the percentage limitation will be 55 percent, for taxable years beginning after Dec. 31, 1983, the percentage limitation will be 60 percent, and thereafter the percentage limitation will be 65 percent.

That Act did not affect the percentage—80 percent—of gross income that must be derived from Virgin Islands sources.

its U.S. tax liability. Although there is some dispute about the underlying tax liability of the recipient of passive investment income from the Virgin Islands, it is the Internal Revenue Service's position that the recipient is liable for the tax (Rev. Rul. 78–327, 1978–2 C.B. 196).[2]

In addition, there is a dispute about the authority of the Virgin Islands to require withholding of this tax (as opposed to the authority to impose the underlying tax). This dispute has been the subject of litigation. The U.S. Court of Appeals for the Third Circuit held that the Virgin Islands did not have the power to impose withholding.[3] The basis of this decision was a Treasury Regulation that provided that U.S. persons were not required to withhold on payments of passive investment income to V.I. persons: the Third Circuit mirrored that Regulation to hold that V.I. persons did not have to withhold on payments to U.S. persons. The Treasury Department has since revoked the underlying Regulation. Therefore, according to the IRS, V.I. persons who pay passive income to U.S. persons must withhold tax at a 30-percent rate. However, some persons have questioned the validity of the IRS revocation of that underlying Regulation. The revocation occurred simultaneously with issuance of a Revenue Procedure that continued the rule that U.S. persons need not withhold on payments of passive investment income to V.I. persons. Therefore, some persons allege that the revocation of the Regulation was a sham and that the Virgin Islands does not have the power to require withholding of the tax. It is understood that these issues are again in controversy.

***Guamanian taxation of passive income***

Like the Virgin Islands, Guam is a possession of the United States and has a tax system generally mirroring the Internal Revenue Code. Until 1972, passive investment income paid by Guamanian persons to U.S. persons was subject to a 30-percent Guamanian tax. As is the case with V.I. taxes today, this tax was creditable (subject to limits) against U.S. tax liability through the foreign tax credit mechanism. In 1972, finding that the effect of the Guamanian passive income tax had been to discourage U.S. investment in Guam, Congress repealed the tax.[4]

### *Reasons for Change*

The current 30-percent tax on the gross amount of passive investment income paid by V.I. persons to U.S. persons discourages investment by U.S. persons in the Virgin Islands. Because no deductions are allowed, the tax on this income, in many cases, is higher than the regular corporate or individual tax would be if deductions were allowed. Although the United States allows a foreign tax credit for taxes paid to the Virgin Islands, such credits cannot offset U.S. tax on U.S. source income. Therefore, the 30-percent tax

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[2] No inference should be drawn from this discussion as to the correctness of the view of either party about this dispute or about the dispute as to the related withholding obligation.

[3] *Vitco* v. *Government of the Virgin Islands*, 560 F. 2d 180 (3d Cir. 1977), *cert. denied*, 435 U.S. 180 (1978).

[4] Congress method of repealing the Guamanian tax was to repeal the 30-percent U.S. tax on passive investment income paid by U.S. persons to Guamanian persons. Repeal of the Guamanian tax thus occurred through "mirroring" of repeal of the U.S. tax.

on gross V.I. source passive investment income frequently results in such income being taxed at a higher rate than similar income earned by U.S. persons in the United States. This disincentive has had the effect of retarding investments by U.S. persons in the Virgin Islands. The Committee has limited the effect of the bill to certain U.S. persons, because the Committee does not intend to enable foreign persons to use the Virgin Islands as a conduit to make investments in the United States.

### *Explanation of Provisions*

The bill will generally limit the Virgin Islands tax on certain passive investment-type income from sources within the Virgin Islands that is not effectively connected with the conduct of a trade or business in the Virgin Islands and that is received by U.S. citizens, resident aliens of the United States, and U.S. corporations, to 10 percent of the gross amount received. The bill will continue the current 30-percent rate for dividends paid to such persons out of earnings and profits accumulated during taxable years beginning before the effective date (the day after the date of enactment). It will treat post-effective date dividends as first coming out of earnings and profits accumulated during taxable years beginning before the effective date.

The bill will allow the Government of the Virgin Islands, in its discretion, further to reduce this 10 percent rate (or to eliminate the tax altogether). The Government of the Virgin Islands will have the discretion to reduce (or eliminate) the tax on the basis of criteria it chooses. The bill will also limit the complementary withholding tax on such income to the reduced 10 percent (or lower) rate.

The reduced rate of tax is available only to U.S citizens, resident aliens and corporations. The bill will not effect the tax treatment of payments by V.I. persons to non-U.S. persons, to U.S. trusts, estates, or partnerships, or to V.I. inhabitants.

The bill makes clear the Virgin Islands' right both to impose the tax and to collect it by requiring withholding.

### *Effective Date*

The reduction in Virgin Islands tax rates will generally apply to amounts received after the date of enactment. However, the withholding obligation will apply to payments made after the date of enactment.

## III. EFFECT OF THE BILL ON THE BUDGET AND VOTE OF THE COMMITTEE IN REPORTING THE BILL

### *Budget effects*

In compliance with clause 7 or Rule XIII of the Rules of the House of Representatives, the following statement is made about the effect on the budget of this bill, H.R. 7093. The committee estimates that the provisions contained in the bill, H.R. 7093, will have a negligible revenue effect.

The Treasury Department agrees with this statement.

***Vote of the committee***

In compliance with clause 2(l)(2)(B) of Rule XI of the Rules of the House of Representatives, the following statement is made about the vote of the committee on the motion to report the bill, as amended. The bill, H.R. 7093, was ordered favorably reported by voice vote.

## IV. OTHER MATTERS TO BE DISCUSSED UNDER HOUSE RULES

In compliance with clauses 3(l)(3) and 2(l)(4) of Rule XI of the Rules of the House of Representatives, the following statement are made with respect to the committee action on H.R. 7093.

***Oversight findings***

With respect to subdivision (A) of clause 2(l)(3) (relating to oversight findings), the committee advises that it was as a result of the committee's oversight activities with respect to taxation of income from sources within the Virgin Islands that the committee concluded that it is appropriate to enact the provisions contained in the bill.

The Subcommittee on Select Revenues Measures of the Committee on Ways and Means held a hearing on the subject (H.R. 6985) on July 12, 1982.

***New budget authority and tax expenditures***

With respect to subdivision (B) of clause 2(l)(3), after consultation with the Director of the Congressinal Budget Office, the committee states that the changes made to existing law by this bill involve no new budget authority or new or increased tax expenditures.

***Consultation with congressional budget officials on budget estimates***

With respect to subdivision (C) of clause 2(l)(3), the committee advises that the Director of the Congressional Budget Office has examined the committee's budget estimates (as indicated in part III of this report) and agrees with the committee's budget estimates.

***Oversight by Committee on Government Operations***

With respect to subdivision (D) of clause 2(l)(3), the committee advises that no oversight findings or recommendations have been submitted to the committee by the Committee on Government Operations regarding the subject matter of this bill.

***Inflationary impact***

In compliance with clause 2(l)(4), the committee states that the enactment of this bill is not expected to have an inflationary impact on prices and costs in the operation of the national economy.

## V. CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3 of Rule XIII of the Rules of the House of Representtives, changes in existing law made by the bill,

as reported, are shown as follows (new matter is printed in italics, existing law in which no change is proposed is shown in roman):

## INTERNAL REVENUE CODE OF 1954

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## Subtitle A—Income Taxes

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## CHAPTER 1—NORMAL TAXES AND SURTAXES

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## Subchapter N—Tax Based on Income From Sources Within or Without the United States

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### PART III—INCOME FROM SOURCES WITHOUT THE UNITED STATES

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### Subpart D—Possessions of the United States

Sec. 931. Income from sources within possessions of the United States.
Sec. 932. Citizens of possessions of the United States.
Sec. 933. Income from sources within Puerto Rico.
Sec. 934. Limitation on reduction in income tax liability incurred to the Virgin Islands.
*Sec. 934A. Reduction in income tax rate on Virgin Islands source income.*

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**SEC. 934. LIMITATION ON REDUCTION IN INCOME TAX LIABILITY INCURRED TO THE VIRGIN ISLANDS.**

(a) GENERAL RULE.—Tax liability incurred to the Virgin Islands pursuant to this subtitle, as made applicable in the Virgin Islands by the Act entitled "An Act making appropriations for the naval service for the fiscal year ending June 30, 1922, and for other purposes", approved July 12, 1921 (48 U. S. C. 1397), or pursuant to section 28(a) of the Revised Organic Act of the Virgin Islands, approved July 22, 1954 (48 U. S. C. 1642), shall not be reduced or remitted in any way, directly or indirectly, whether by grant, subsidy, or other similar payment, by any law enacted in the Virgin Island, except to the extent provided in subsection (b) or (c) *or in section 934A*.

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***SEC. 934A. REDUCTION IN INCOME TAX RATE ON VIRGIN ISLANDS SOURCE INCOME.***

*(a) GENERAL RULE.—For purposes of determining the tax liability incurred by citizens and resident alien individuals of the United States, and corporations organized in the United States, to the*

*Virgin Islands pursuant to this title with respect to amounts received from sources within the Virgin Islands—*

*(1) the rate of the taxes imposed by sections 871(a)(1) and 881 shall not exceed 10 percent, and*

*(2) subsection (a) of section 934 shall not apply to such taxes.*

*(b) REDUCED RATES NOT TO APPLY TO PRE-EFFECTIVE DATE EARNINGS.—*

*(1) IN GENERAL.—The reduction under subsection (a)(1), and any reduction under section 934 pursuant to subsection (a)(2), in a rate of tax imposed by section 871(a)(1) or 881 shall not apply to dividends paid out of earnings and profits accumulated for taxable years beginning before the effective date of the reduction.*

*(2) ORDERING RULE.—For purposes of paragraph (1), dividends shall be treated as first being paid out of earnings and profits accumulated for taxable years beginning before the effective date of the reduction (to the extent thereof).*

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## CHAPTER 3—WITHHOLDING OF TAX ON NONRESIDENT

## ALIENS AND FOREIGN CORPORATIONS AND TAX-FREE COVENANT BONDS

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### Subchapter A—Nonresident Aliens and Foreign Corporations

Sec. 1441. Withholding of tax on nonresident aliens.
Sec. 1442. Withholding of tax on foreign corporations.
Sec. 1443. Foreign tax-exempt organizations.
*Sec. 1444. Withholding on Virgin Islands source income.*

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***SEC. 1444. WITHHOLDING ON VIRGIN ISLANDS SOURCE INCOME.***

*For purposes of determining the withholding tax liability incurred to the Virgin Islands pursuant to this title with respect to amounts received from sources within the Virgin Islands by citizens and resident alien individuals of the United States, and corporations organized in the United States, the rate of withhholding tax under sections 1441 and 1442 on income subject to tax under section 871(a)(1) or 881 shall not exceed the rate of tax on such income under section 871(a)(1) or 881; as the case may be.*

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97TH CONGRESS } HOUSE OF REPRESENTATIVES { REPORT
2d Session } { No. 97-836

# COMPUTER EQUIPMENT CONTRIBUTION ACT OF 1982

SEPTEMBER 17, 1982.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. ROSTENKOWSKI, from the Committee on Ways and Means, submitted the following

## REPORT

[To accompany H.R. 5573]

[Including cost estimate of the Congressional Budget Office]

The Committee on Ways and Means, to whom was referred the bill (H.R. 5573) to amend the Internal Revenue Code of 1954 to encourage contributions of computers and other sophisticated technological equipment to elementary and secondary schools, having considered the same, report favorably thereon with amendments and recommend that the bill as amended do pass.

The amendments are as follows:

Strike out all after the enacting clause and insert in lieu thereof the following:

SECTION 1. SHORT TITLE.

This Act may be cited as the "Computer Equipment Contribution Act of 1982".

SEC. 2. CHARITABLE CONTRIBUTIONS OF COMPUTER EQUIPMENT TO PRIMARY AND SECONDARY SCHOOLS.

Subsection (e) of section 170 of the Internal Revenue Code of 1954 (relating to certain contributions of ordinary income and capital gain property) is amended by adding at the end thereof the following new paragraph:

"(5) SPECIAL RULE FOR CONTRIBUTIONS OF COMPUTER EQUIPMENT TO PRIMARY AND SECONDARY SCHOOLS.—

"(A) LIMIT ON REDUCTION.—In the case of a qualified contribution of computer equipment, the reduction under paragraph (1)(A) shall be no greater than the amount determined under paragraph (3)(B).

"(B) QUALIFIED CONTRIBUTION OF COMPUTER EQUIPMENT.—For purposes of this paragraph, the term 'qualified contribution of computer equipment' means a charitable contribution by a corporation of tangible personal property described in paragraph (1) of section 1221, but only if—

"(i) the contribution is to a qualified educational organization and is made through the governing body of such organization,

"(ii) the contribution is made pursuant to a written plan of the taxpayer under which there will not be undue concentrations of the taxpayer's contributions of computer equipment from the geographic standpoint or from the standpoint of the relative economic status of the donees' students,

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"(iii) the property is assembled by the taxpayer and the taxpayer is regularly engaged in the business of assembling and selling computer equipment of the same kind as such property,

"(iv) the contribution is made—

"(I) not later than 6 months after the date the assembly of the property is substantially completed, and

"(II) during 1983,

"(v) the original use of the property is by the donee,

"(vi) the property is computer equipment substantially all the use of which by the donee will be at the institution directly in the education of students,

"(vii) the property is not transferred by the donee in exchange for money, other property, or services, and

"(viii) the taxpayer receives from the donee a written statement representing that its use and disposition of the property will be in accordance with the provisions of clauses (vi) and (vii).

"(C) QUALIFIED EDUCATIONAL ORGANIZATIONS.—For purposes of this paragraph, the term 'qualified educational organization' means—

"(i) an educational organization which is described in subsection (b)(1)(A)(ii), and

"(ii) a school operated as an activity of an organization described in section 501(c)(3) and exempt from income tax under section 501(a) if such school normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on.

Such term shall not included any institution of higher education (as defined in section 3304(f)) and shall not include any organization not located in the United States.

"(D) COMPUTER EQUIPMENT.—For purposes of this paragraph, the term 'computer equipment' means—

"(i) a data processor which—

"(I) can be programmed in at least 3 standard computer languages,

"(II) has a random access memory with a capacity for at least 32,000 bytes, and

"(III) is (or can be) connected with a screen for visual display of the data,

"(ii) if donated by the taxpayer for use in connection with a data processor described in clause (i) donated by the taxpayer—

"(I) a display screen,

"(II) a printer, or

"(III) a disc drive, and

"(iii) any installation equipment for equipment described in clause (i) or (ii).

"(E) CORPORATION.—For purposes of this paragraph, the term 'corporation' shall not include—

"(i) an electing small business corporation (as defined in section 1371(b)),

"(ii) a personal holding company (as defined in section 542), and

"(iii) a service organization (as defined in section 414(m)(3))."

SEC. 3. EFFECTIVE DATE.

The amendment made by section 2 shall apply to taxable years ending after December 31, 1982.

Amend the title so as to read: "A bi'l to amend the Internal Revenue Code of 1954 to encourage contributions of computer equipment to elementary and secondary schools."

## I. SUMMARY

The bill provides a special rule for charitable contributions, made by corporations in 1983, of certain newly manufactured computers to primary or secondary schools for use at the school directly in the education of students. For contributions qualifying under the rule, the deduction equals the sum of the taxpayer's basis in the donated property plus 50 percent of the difference between the property's fair market value and the basis, but not to exceed twice the basis amount.

## II. EXPLANATION OF THE BILL

### *Present Law*

***General reduction rule***

The amount of a charitable deduction otherwise allowable for donated property generally must be reduced by the amount of any ordinary income which the donor would have realized had the property been sold for its fair market value at the date of the contribution (Code sec. 170(e)). Thus, a donor of appreciated ordinary-income property (property the sale of which would not give rise to long-term capital gain) generally may deduct only the donor's basis in the property, rather than the fair market value. For example, a manufacturer which donates a product from its inventory generally may deduct only its cost for the item.

***Special rule for certain corporate contributions***

A different rule applies to charitable contributions by corporations of two types of ordinary-income property if donated to certain exempt organizations for specified purposes. The special rule applies to corporate donations of ordinary-income property to a charitable organization to be used solely for care of the needy, the ill, or infants (such as donations by the producer or manufacturer of food, clothing, or medical equipment), where such use is related to the donee's charitable functions (sec. 170(e)(3)). Also, the special rule applies to corporate donations of newly manufactured scientific equipment to a college or university to be used for research (or research training) in the United States in the physical or biological sciences (sec. 170(e)(4)).

In these cases, the corporate donor is allowed a deduction equal to the sum of its basis in the property plus one-half of the unrealized appreciation (i.e., the difference between fair market value and basis), but not in excess of twice the basis.

### *Reasons for Change*

The committee believes that an additional incentive would be desirable to encourage manufacturers to contribute computers to secondary and primary schools for use at the school directly in the education of students, so that young students will become trained in today's technology. Skill in using computers has become essential as more and more jobs require computer literacy.

The desirability of making available computers to schoolchildren makes it appropriate to provide, for a limited time, a greater tax incentive than in present law for contributions of computers, manufactured by the donor corporation no more than six months before contribution, which the donee school uses directly in the education of students. The committee also believes that the deduction so allowed should not be such that the donor corporation could be in a better after-tax situation by donating the property than by selling it. Accordingly, the increased charitable deduction allowed by the bill could not exceed twice the amount of the taxpayer's basis in the donated computer equipment.

## *Explanation of Provisions*

### *Overview*

The bill provides a special deduction rule for charitable contributions, made by corporations in 1983, of certain newly manufactured computers to primary or secondary schools for the use at the school directly in the education of students.

The principal intended beneficiary of the bill is Apple Computer, Inc. The provisions of the bill will also benefit any other corporate taxpayer which, during 1983, makes qualifying charitable contributions of computer equipment.

### *Requirements for favorable treatment*

In order for the special deduction rule to apply, there must be a charitable contribution [1] by a corporation [2] of tangible personal property which satisfies all of the following requirements.

*1. Qualifying computer equipment*

The donated property must be tangible personal property which is inventory (within the meaning of sec. 1221(1)) and must be computer equipment as defined in the bill. Also, the computer equipment must be assembled by the taxpayer, and the taxpayer must be regularly engaged in the business of assembling and selling such equipment.

The bill defines computer equipment qualifying for the special deduction rule to mean—

(1) a data processor which can be programmed in at least three standard computer languages, which has a random access memory with a capacity for at least 32,000 bytes (determined by reference to the donated computer equipment, without regard to additional random access memory capacity which could be achieved through use of additional equipment which is not donated), and which is (or can be) connected with a screen for visual display of the data;

(2) a display screen, a printer, or a disc drive, but only if such equipment is donated by the taxpayer for use in connection with such a data processor donated by the taxpayer; and

(3) any installation equipment for equipment, donated by the taxpayer, which is described in (1) or (2). The term installation equipment is limited to cables and display screen, printer, or cassette recorder "hook up" equipment such as modulators, interface boards, or interface cards.

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[1] Court cases have held that if a transfer to a charitable organization results in a benefit to the donor, no charitable deduction is allowed. For example, the U.S. Court of Claims has upheld denial of charitable deductions claimed by a manufacturer for discounts on purchases of sewing machines by schools, where the court had found that the discounts were offered for the predominant purpose of enlarging the market for the manufacturer's brand of sewing machines (*Singer Co.* v. *U.S.*, 449 F.2d 413 (Ct. Cl. 19 1)). In the case of qualifying contributions of computer equipment under the bill, the committee intends that such computer equipment contributions are to be treated as charitable contributions without regard to the donor-benefit rule expressed in the *Singer* case.

[2] The special deduction rule does not apply in the case of a corporation which is a subchapter S corporation, as defined in sec. 1371(b); a personal holding company, as defined in sec. 542; or a service organization, as defined in sec. 414(m)(3).

Intangible computer property and tangible property which is not expressly listed in the bill's definition of computer equipment does not qualify for the special deduction rule under the bill.

*2. Eligible donees*

The computer equipment must be donated either to an educational organization (within the meaning of sec. 170(b)(1)(A)(ii)),[3] or to a primary or secondary school operated as an activity of a tax-exempt section 501(c)(3) organization (such as a church), provided that such school normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on. Also, the donee must be located in the United States and may not be an institution of higher education (as defined in sec. 3304(f)).[4] Under the bill, a State-run public vocational or technical education school (which is an educational organization within the meaning of sec. 170(b)(1)(A)(ii)) is an eligible donee if the school admits students who have not either graduated from high school or earned a high school equivalency certificate.

*3. Governing body*

The contribution of computer equipment to an eligible donee must be made through the donee's governing body.

For example, where State law provides that a local school board or school district has the authority to accept and administer charitable gifts for public schools under the jurisdiction of the board or district, the contribution must be made through such governing body. In the case of a private school, the contribution must be made through the school's board of trustees or other governing body.

*4. Time of contribution*

The contribution must be made within six months after substantial completion of construction of the computer equipment, and must be made during the calendar year 1983.

*5. Limitation to new equipment*

The original use of the donated computer equipment must be by the donee.

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[3] An educational organization is described in sec. 170(b)(1)(A)(ii) "if its primary function is the presentation of formal instruction and it normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on. The term includes institutions such as primary, secondary, preparatory, or high schools, * * *" and includes both public and private schools (Reg. § 1.170A-9(b)(1)).

[4] An institution of higher education, as defined in sec. 3304(f), means an educational institution which (1) admits as regular students only individuals having a certificate of graduation from a high school, or the recognized equivalent of such a certificate; (2) is legally authorized to provide a program of education beyond high school; (3) provides an educational program for which it awards a bachelor's or higher degree, provides a program which is acceptable for full credit toward a degree, or offers a program of training to prepare students for gainful employment in a recognized occupation; and (4) is a public or other nonprofit institution.

*6. Student education use requirement*

Substantially all (at least 80 percent) of the use of the donated computer equipment by the donee is at the location of the donee and is directly in the education of students.

*7. Prohibition on donee sale*

The donated computer equipment may not be transferred by the donee in exchange for money, other property, or services.

*8. Written confirmation*

The donor corporation must receive a written statement from the donee representing that the use and disposition of the donated computer equipment will be in accordance with the preceding two requirements.

*9. Distributional requirements*

The contribution must be made pursuant to a written plan of the donor corporation under which there will not be undue concentrations of the donor's contributions of computer equipment from either a geographic standpoint or from the standpoint of the relative economic status of the students of the donees which receive contributions from the donor. These distributional requirements are intended to insure a widespread distribution of donated property which will benefit a wide cross-section of students. There is no intention to require the taxpayer to distribute computer equipment to every State or to each geographical region of the United States.

A determination of whether a donor's contribution plan meets these distributional requirements is to be made on an overall basis, taking into account all the donees which receive contributions from the donor under the plan (not just certain of such donees). If under a plan contributions are made through one or more governing bodies which have authority to allocate contributed equipment to particular schools under the body's jurisdiction (e.g., as where a school district allocates donated computer equipment only to its high schools), then a determination of whether the plan meets the distributional requirement as to a relative economic status of students is to be made by taking into account the relative economic status of students of all schools within the jurisdiction of the governing body.

***Allowable deduction***

If all the requirements of the bill are satisfied, the charitable deduction allowed by the bill generally is for the sum of (1) the taxpayer's basis in the property, plus (2) one-half of the unrealized appreciation (i.e., one-half of the difference between the property's fair market value [5] determined at the time of the contribution and the donor's basis in the property).

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[5] Where donated prperty is of a type which the taxpayer sells in the course of its business, the fair market value is the price which the taxpayer would have received if the taxpayer had sold the contributed property in the usual market in which it customarily sells, at the time and place of the contribution, and, in the case of a contribution of goods in quantity, in the quantity contributed. The usual market of a manufacturer or other producer consists of the wholesalers or other distributors to or through whom it customarily sells; but if it sells only at retail, the usual market consists of its retail customers (Reg. § 170A–1(c)(2)).

However, in no event is a deduction allowed for any amount in excess of twice the basis of the property. For example, if a manufacturer makes a qualifying contribution of a computer with a cost basis of $\$5X$, and a fair market value of $\$16X$, the bill allows the manufacturer a charitable deduction of $\$10X$ (twice the $\$5X$ basis, since that amount is less than basis plus one-half of the unrealized appreciation). If instead the fair market value of the computer is $\$11X$, the deduction would be $\$8X$ ($\$5X$ basis plus one-half of the $\$6X$ difference between value and basis).

### *Effective Date*

The special deduction rule provided by the bill will apply to taxable years ending after 1982.

## III. EFFECT OF THE BILL ON THE BUDGET AND VOTE OF THE COMMITTEE IN REPORTING THE BILL

### *Budget Effects*

In compliance with clause 7 of Rule XIII of the Rules of the House of Representatives, the following statement is made about the effect on the budget of this bill, H.R. 5573. The committee estimates that the provisions contained in the bill, H.R. 5573, as amended, will reduce fiscal year budget receipts by $15 million in 1983, $21 million in 1984, and a negligible amount in 1985.

The Treasury Department agrees with this statement.

### *Vote of the Committee*

In compliance with clause 2(l)(2)(B) of Rule XI of the Rules of the House of Representatives, the following statement is made about the vote of the committee on the motion to report the bill, as amended. The bill, as amended, was initially approved by a record vote of 20–3, with 7 votes being cast by proxy. Subsequently, the full committee was polled and agreed that the bill should be placed on the suspension calendar.

## IV. OTHER MATTERS TO BE DISCUSSED UNDER HOUSE RULES

In compliance with clauses 3(l)(3) and 2(l)(4) of Rule XI of the Rules of the House of Representatives, the following statements are made with respect to the committee action on H.R. 5573, as amended.

### *Oversight Findings*

With respect to subdivision (A) of clause 2(l)(3) (relating to oversight findings), the committee advises that it was a result of the committee's oversight activities with respect to Federal income tax deductions for charitable contributions of property, such as computer equipment, that the committee concluded that it is appropriate to enact the provisions contained in the bill. The Subcommittee on Select Revenue Measures held a hearing on the bill, H.R. 5573, on June 14, 1982, and ordered the bill favorably reported on July 12, 1982, with amendments. The Subcommittee transmitted a report to the full committee on September 10, 1982.

### *New Budget Authority and Tax Expenditures*

With respect to subdivision (B) of clause 2(l)(3), after consultation with the Director of the Congressional Budget Office, the committee states that the changes made to existing law by this bill involve no new budget authority or new tax expenditures, but involve in-

creased tax expenditures. The estimated effect on budget receipts of the changes made to existing law by the bill are shown in part III of this report.

### *Consultation with Congressional Budget Officials on Budget Estimates*

With respect to subdivision (C) of clause 2(l)(3), the committee advises that the Director of the Congressional Budget Office has examined the committee's budget estimates (as indicated in part III of this report) and submitted the following statement:

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
*Washington, D.C.*

Hon. DAN ROSTENKOWSKI,
*Chairman, Committee on Ways and Means,*
*House of Representatives, Washington, D.C.*

DEAR MR. CHAIRMAN: In accordance with the Budget Act, the Congressional Budget Office has examined H.R. 5573, the Technology Education Act of 1982. This bill provides a special deduction rule for charitable contributions made by corporations in 1983 of certain newly manufactured computers to primary and secondary schools.

This bill does not provide any new budget authority or any new tax expenditures. However, the bill does increase tax expenditures.

In accordance with Section 403 of the Budget Act, the Congressional Budget Office estimates that the bill will reduce budget receipts and increase tax expenditures by $15 million in fiscal year 1983, $21 million in fiscal year 1984, and by a negligible amount in fiscal year 1985.

Sincerely,

RAYMOND C. SCHEPPACH
(For Alice M. Rivlin, Director).

### *Oversight by Committee on Government Operations*

With respect to subdivision (D) of clause 2(l)(3), the committee advises that no oversight findings or recommendations have been submitted to the committee by the Committee on Government Operations regarding the subbject matter of this bill.

### *Inflationary Impact*

In compliance with clause 2(l)(4), the committee states that the enactment of this bill is not expected to have an inflationary impact on prices and costs in the operation of the national economy.

## V. CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3 of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (new matter is printed in italic, existing law in which no change is proposed is shown in roman):

## SECTION 170 OF THE INTERNAL REVENUE CODE OF 1954

### SEC. 170. CHARITABLE, ETC., CONTRIBUTIONS AND GIFTS.

(a) ALLOWANCE OF DEDUCTION.—* * *

* * * * * * *

(e) CERTAIN CONTRIBUTIONS OF ORDINARY INCOME AND CAPITAL GAIN PROPERTY.—

(1) GENERAL RULE.—The amount of any charitable contribution of property otherwise taken into account under this section shall be reduced by the sum of—

(A) the amount of gain which would not have been long-term capital gain if the property contributed has been sold by the taxpayer at its fair market value (determined at the time of such contribution), and

(B) in the case of a charitable contribution—

(i) of tangible personal property, if the use by the donee is unrelated to the purpose or function constituting the basis for its exemption under section 501 (or, in the case of a governmental unit, to any purpose or function described in subsection (c)), or

(ii) to or for the use of a private foundation (as defined in section 509(a)), other than a private foundation described in subsection (b)(1)(D),

40 percent ($^{28}/_{46}$ in the case of a corporation) of the amount of gain which would have been long-term capital gain if the property contributed had been sold by the taxpayer at its fair market value (determined at the time of such contribution). For purposes of applying this paragraph (other than in the case of gain to which section 617(d)(1), 1245(a), 1250(a), 1251(c), 1252(a), or 1254(a) applies), property which is property used in the trade or business (as defined in section 1231(b)) shall be treated as a capital asset.

(2) ALLOCATION OF BASIS.—For purposes of paragraph (1), in the case of a charitable contribution of less than the taxpayer's entire interest in the property contributed, the taxpayer's adjusted basis in such property shall be allocated between the interest contributed and any interest not contributed in accordance with regulations prescribed by the Secretary.

(3) SPECIAL RULE FOR CERTAIN CONTRIBUTIONS OF INVENTORY AND OTHER PROPERTY.—

(A) QUALIFIED CONTRIBUTIONS.—For purposes of this paragraph, a qualified contribution shall mean a charitable contribution of property described in paragraph (1) or (2) of section 1221, by a corporation (other than a corporation which is an electing small business corporation within the meaning of section 1371(b)) to an organization which is described in section 501(c)(3) and is exempt under section 501(a) (other than a private foundation, as defined in section 509(a), which is not an operating foundation, as defined in section 4942(j)(3), but only if—

(i) the use of the property by the donee is related to the purpose or function constituting the basis for its exemption under section 501 and the property is to be used by the donee solely for the care of the ill, the needy, or infants;

(ii) the property is not transferred by the donee in exchange for money, other property, or services;

(iii) the taxpayer receives from the donee a written statement representing that its use and disposition of the property will be in accordance with the provisions of clauses (i) and (ii); and

(iv) in the case where the property is subject to regulation under the Federal Food, Drug, and Cosmetic Act, as amended, such property must fully satisfy the applicable requirements of such Act and regulations promulgated thereunder on the date of transfer and for one hundred and eighty days prior thereto.

(B) AMOUNT OF REDUCTION.—The reduction under paragraph (1)(A) for any qualified contribution (as defined in subparagraph (A)) shall be no greater than the sum of—

(i) one-half of the amount computed under paragraph (1)(A) (computed without regard to this paragraph), and

(ii) the amount (if any) by which the charitable contribution deduction under this section for any qualified contribution (computed by taking into account the amount determined in clause (i), but without regard to this clause) exceeds twice the basis of such property.

(C) This paragraph shall not apply to so much of the amount of the gain described in paragraph (1)(A) which would be long-term capital gain but for the application of sections 617, 1245, 1250, 1251, or 1252.

(4) SPECIAL RULE FOR CONTRIBUTIONS OF SCIENTIFIC PROPERTY USED FOR RESEARCH.—

(A) LIMIT ON REDUCTION.—In the case of a qualified research contribution, the reduction under paragraph (1)(A) shall be no greater than the amount determined under paragraph (3)(B).

(B) QUALIFIED RESEARCH CONTRIBUTIONS.—For purposes of this paragraph, the term "qualified research contribution" means a charitable contribution by a corporation of tangible personal property described in paragraph (1) of section 1221, but only if—

(i) the contribution is to an educational organization which is described in subsection (b)(1)(A)(ii) of this section and which is an institution of higher education (as defined in section 3304(f)),

(ii) the property is constructed by the taxpayer,

(iii) the contribution is made not later than 2 years after the date the construction of the property is substantially completed,

(iv) the original use of the property is by the donee,

(v) the property is scientific equipment or apparatus substantially all of the use of which by the donee is for research or experimentation (within the meaning of section 174), or for research training, in the United States in physical or biological sciences,

(vi) the property is not transferred by the donee in exchange for money, other property, or services, and

(vii) the taxpayer receives from the donee a written statement representing that its use and disposition of the property will be in accordance with the provisions of clauses (v) and (vi).

(C) CONSTRUCTION OF PROPERTY BY TAXPAYER.—For purposes of this paragraph, property shall be treated as constructed by the taxpayer only if the cost of the parts used in the construction of such property (other than parts manufactured by the taxpayer or a related person) do not exceed 50 percent of the taxpayer's basis in such property.

(D) CORPORATION.—For purposes of this paragraph, the term "corporation" shall not include—

(i) an electing small business corporation (as defined in section 1371(b)),

(ii) a personal holding company (as defined in section 542), and

(iii) a service organization (as defined in section 414 (m)(3)).

*(5) Special rule for contributions of computer equipment to primary and secondary schools.—*

*(A) LIMIT ON REDUCTION.—In the case of a qualified contribution of computer equipment, the reduction under paragraph (1)(A) shall be no greater than the amount determined under paragraph (3)(B).*

*(B) QUALIFIED CONTRIBUTION OF COMPUTER EQUIPMENT.—For purposes of this paragraph, the term "qualified contribution of computer equipment" means a charitable contribution by a corporation of tangible personal property described in paragrah (1) of section 1221, but only if—*

*(i) the contribution is to a qualified educational organization and is made through the governing body of such organization,*

*(ii) the contribution is made pursuant to a written plan of the taxpayer under which there will not be undue concentrations of the taxpayer's contributions of computer equipment from the geographic standpoint or from the standpoint of the relative economic status of the donees' students,*

*(iii) the property is assembled by the taxpayer and the taxpayer is regularly engaged in the business of assembling and selling computer equipment of the same kind as such property,*

*(iv) the contribution is made—*

*(I) no later than 6 months after the date of the assembly of the property is substantially completed, and*

*(II) during 1983,*

*(v) the original use of the property is by the donee,*

*(vi) the property is computer equipment substantially all the use of which by the donee will be at the institution directly in the education of students,*

*(vii) the property is not transferred by the donee in exchange for money, other property or services, and*

*(viii) the taxpayer receives from the donee a written statement representing that its use and disposition of the property will be in accordance with the provisions of clauses (vi) and (vii).*

*(C) QUALIFIED EDUCATIONAL ORGANIZATIONS.—For purposes of this paragraph, the term "qualified educational organization" means—*

*(i) an educational organization which is described in subsection (b)(1)(A)(ii), and*

*(ii) a school operated as an activity of an organization described in section 501(c)(3) and exempt from income tax under section 501(a) if such school normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on.*

*Such term shall not include any institution of higher education (as defined in section 3304(f)) and shall not include any organization not located in the United States.*

*(D) COMPUTER EQUIPMENT.—For purposes of this paragraph, the term "computer equipment" means—*

*(i) a data processor which—*

*(I) can be programmed in at least 3 standard computer languages,*

*(II) has a random access memory with a capacity for at least 32,000 bytes, and*

*(III) is (or can be) connected with a screen for visual display of the data,*

*(ii) if donated by the taxpayer for use in connection with a data processor described in clause (i) donated by the taxpayer—*

*(I) a display screen,*

*(II) a printer, or*

*(III) a disc drive, and*

*(iii) any installation equipment for equipment described in clause (i) or (ii).*

*(E) CORPORATION.—For purposes of this paragraph, the term "corporation" shall not include—*

*(i) an electing small business corporation (as defined in section 1371(b)),*

*(ii) a personal holding company (as defined in section 542), and*

*(iii) a service organization (as defined in section 414(m)(3)).*

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